



California Tax Reform Association

717 K St, Ste 510, Sacramento, CA 95814

Ph: 916.446.4300 Fax: 916.444.6611

Email: info@caltaxreform.org

<http://www.caltaxreform.org>

To: Air Resources Board

From: Lenny Goldberg, TURN and CTRA

Re: Early Action Measures: Carbon Fee phase-in

One of the most effective early actions that CARB could take in discouraging carbon emissions would be to announce the imposition of a carbon permit fee, one that would phase in beginning in 2008 or as soon as practical and increase to a significant level—say, \$20/ton of carbon emission--by 2010. The authority for this fee is contained in section 38597 of AB 32.

The early announcement of a carbon fee will enlist the appropriately touted “genius of the market” without any regulatory burden or bureaucratic requirements. It will lower carbon emissions through millions of discrete actions, taken by millions of individuals and businesses, all of which will be motivated by avoiding upcoming costs. To the extent that a fee is known to be coming and known to be increasing over time, people and businesses can make plans to lower their carbon emissions and therefore their costs, whether through changing consumption patterns, retrofitting their business operations, or ending wasteful activities—without any regulatory proceedings.

We do not view the fee as a substitute for regulatory activities. Regulation must identify those specific measures which can generate mandated emission reductions and, of course, must define and enforce the carbon cap. But a fee is a way of getting way beyond the limited reach of regulatory mechanisms into the cumulative millions of decisions of the everyday lives of our citizens. Since costs affect behavior, then a fee on carbon-emitting activities would appropriately affect behavior by promoting carbon emission reductions.

At one of the first Action Team meetings, we requested simply a public discussion of this issue. While discussions have taken place in the legislature, we urge that the ARB place discussion of a carbon fee on its agenda of upcoming early action items.

Phase 1: A fee to build the AB 32 program and to test implementation

Section 38597 of AB 32 permits a carbon permit fee for “the purposes of the division”, which is to control global warming. At minimum, there is no dispute over the ability of the state to charge a fee for program implementation.

To do so would have immediate impacts. First, the best possible program could be put in place and would be fully funded. Early aspects of the program, such as public education about carbon-emitting activity, could be paid for immediately. Any research, data gathering, technical expertise, and other expenses for the program would be self-supporting, subject to legislative scrutiny. There can be no doubt that current funding sources are limited, and that a robust program can and should have its own funding source, subject of course to budgetary oversight. Implementation which meets the rigorous timetables of AB 32 will be more likely to succeed with fee support.

To the extent that there may be some delay in implementing and collecting funds, funding for the AB 32 program can be kept on the books of the current funds as a loan. That would permit full funding of the program, without immediate budgetary constraints, with the knowledge that there will be no risk to other fund sources.

Another important immediate impact is experience with implementation of the fee. If, as the Governor has advocated, there will eventually be a “cap and trade” system which will require permits, then experience in properly assessing, collecting, and enforcing a permit system, with attendant fees, will be necessary. The appropriate placement and collection of the permit fee with regard to upstream and downstream (business and consumer) activities is a major area for discussion. The Board of Equalization will need to develop the experience to administer these fees, and a number of issues (e.g. double-counting, reporting requirements) will need to be worked out in experience. If we start right away with a small fee for the program, those issues will become clearer more quickly.

In terms of those sectors with limited data on carbon emissions, we believe that a fee can be implemented relatively efficiently and rapidly on the two major sectors which release carbon emissions, namely, transportation fuels and electricity. While stationary sources apparently require more data than is currently available, the initial level of the fee will be small, and we would suggest at least a minimum or nominal fee on all emitters, which would develop information and experience with the universe of emissions which eventually will be part of a full-blown permit system.

Phase 2: Planning for the revenue, mitigating impacts: creating a Carbon Fund

As a carbon fee phases in, it will be critical to understand its impacts, and the impacts of the broader program, including regulatory activities. What activities and people will be adversely impacted, in such a way that may require compensation? What level of revenue will be generated, from what sectors and in what manner? What types of innovation can and should be funded which can accelerate the process? What is the distribution of demand for permits, such that an understanding of how an effective trading market based on the purchase of carbon permits can be developed? How quickly will emissions be reduced as the result of what level of carbon fee?

While section 38597 calls for expenditure of revenues by the legislature, the ARB would do well to initiate a broad-based discussion and provide recommendations for the most effective ways of utilizing the revenue. Are there well-placed transit subsidies which can draw more riders out of their cars? Are the impacts of a fee on the poor inappropriately placing a burden on those with a low-carbon footprint? How can fee revenue complement programs which are currently funded by electricity ratepayers? Are there certain industries or activities which require mitigation? What technological innovations hold out the most promise and may need support?

Creating a Carbon Fund with an estimated \$2-\$3 billion yearly from carbon fees (at full implementation) will have enormous impact on the effectiveness of a carbon reduction program. Right now, there are numerous “green” tax credit proposals which, to the extent that they have merit in meeting their goals, would be funded not by the general fund but a Carbon Fund. Many have suggested appropriate tax relief or carbon credits for individuals as means of mitigating the costs of the global warming program. And, of course, there are numerous proposals for new technology and diffusion of innovation which would reduce carbon, many of which require direct expenditures or seed money.

The planning and discussion for expenditures of a Carbon Fund will prove to be one of the most dynamic and challenging activities undertaken by the scientific community, advocacy groups, the Administration and the Legislature. That discussion should start now, and, like other activities under the ARB program, should enlist the creative efforts of the national and world community. However, it cannot occur until and unless the ARB initiates the public discussion of a carbon fee.

Possible Phase 3: implementation of cap and trade: auctioning permits

While cap-and-trade is not considered part of early action, it obviously requires a number of steps before it can be implemented. We have commented separately to the Market Advisory Committee on the issue of auctioning permits as a far more effective way of constructing the market than allocating permits for free.

In this context, it is sufficient to say that, since carbon permits will be the property to be traded, a carbon permit fee system should be developed as soon as possible in order to begin the process of market design. Among many of the issues which have been raised: if large oil and electricity companies control the bulk of the permits, how can a trading regime be a competitive and effective one, free from gaming? How are traded permits tracked and enforced through the market process, with verification that the permits sold mean fewer emissions by the seller and more only by a verified buyer?

Clearly, there are many issues which will have to be addressed to make such a system work. For the purposes of “early action”, the sooner the ARB implements a carbon permit fee, the more likely the information and understanding will be developed to have a successful carbon reduction program.